

Report
of the
Examination of
Vision Care Network Insurance Corporation
Racine, Wisconsin
As of December 31, 2004

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State of Wisconsin / OFFICE OF THE COMMISSIONER OF INSURANCE

Jim Doyle, Governor
Jorge Gomez, Commissioner

Wisconsin.gov

October 4, 2005

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Honorable Jorge Gomez
Commissioner of Insurance
Madison, Wisconsin

Commissioner:

In accordance with your instructions, a compliance examination has been made of
the affairs and financial condition of:

VISION CARE NETWORK INSURANCE CORPORATION
Racine, Wisconsin

and this report is respectfully submitted.

I. INTRODUCTION

The previous examination of Vision Care Network Insurance Corporation (VCN or the company) was conducted in 1999 as of December 31, 1998. The current examination covered the intervening period ending December 31, 2004, and included a review of such 2005 transactions as deemed necessary to complete the examination.

The examination consisted of a review of all major phases of the company's operations and included the following areas:

- History
- Management and Control
- Corporate Records
- Conflict of Interest
- Fidelity Bonds and Other Insurance
- Provider Contracts
- Territory and Plan of Operations
- Growth of the company
- Financial Statements
- Accounts and Records
- Enrollee Complaint Procedure

Emphasis was placed on the audit of those areas of the company's operations accorded a high priority by the examiner-in-charge when planning the examination. Special

attention was given to the action taken by the company to satisfy the recommendations and comments made in the previous examination report.

The section of this report titled "Summary of Examination Results" contains comments and elaboration on those areas where adverse findings were noted or where unusual situations existed. Comment on the remaining areas of the company's operations is contained in the examination work papers.

The company is not annually audited by an independent public accounting firm. The company filed a CPA Audit Exemption Affidavit as prescribed by s. Ins 50.16, Wis. Adm. Code.

II. HISTORY AND PLAN OF OPERATION

The Vision Care Network Insurance Corporation is a for-profit group model limited service health organization (LSHO) insurer. An LSHO insurer is defined by s. 609.01 (3), Wis. Stat., as ". . . a health care plan offered by an organization established under ch. 185, 611, 613, or 614 or issued a certificate of authority under ch. 618 that makes available to its enrolled participants, in consideration for predetermined fixed payments, a limited range of health care services performed by providers selected by the organization." Under the group model, the LSHO contracts with a sponsoring clinic to provide primary and specialist services. LSHOs compete with traditional fee-for-service vision care delivery.

VCN was incorporated August 8, 1989, and commenced business January 1, 1990. Dr. Bruce A. Savin, O.D., is the sole shareholder of the company.

VCN provides subscriber-group member enrollees with covered vision care services through contracts with one provider group, Dr. Savin and Associates d/b/a Vision Clinic, LTD. (Vision Clinic).

The provider contract with Vision Clinic lists separate benefits for a) eligible employees and their dependents and b) eligible retirees and their dependents. Vision Clinic covers the following benefits for eligible employees/eligible dependents:

1. vision examination every 12 months,
2. frames priced up to \$79 retail—replacement allowed every 12 months,
3. lenses every 12 months provided there is a change in the prescription that necessitates the new lenses
4. contact lenses allowance up to \$90 every 12 months.

Also, the eligible employee/eligible dependent can select either one pair of glasses or one pair of contact lenses every 12 months, but not both. Eligible retirees and their eligible dependents have the same benefits except that the benefits are provided once every 24 months as opposed to once every 12 months.

Vision Clinic is reimbursed on a capitation basis for providing benefits to VCN enrollees. A portion of this capitation rate (10%) is for administration services. See the section entitled "Summary of Current Examination Results" for further detail.

The contract includes hold-harmless provisions for the protection of policyholders. In the agreement, Vision Clinic looks solely to VCN for payment of covered services and looks solely

to the enrolled member for payment of noncovered services, including applicable copayments. The contract term is indefinite but may be terminated by written notice of intent to terminate mailed to the other party by certified mail at least 90 days prior to the intended effective date of such termination.

VCN markets to employer groups in Racine County only. VCN uses an outside agent. There is no written agreement between VCN and the agent since VCN is not currently marketing its plan.

VCN has one master contract (service agreement). A consultant developed initial premium rates. Rates are reviewed on an annual basis. There has been one adjustment to the premium rates.

The master contract with the employer contains a paragraph regarding the grievance procedure. Each participant may submit a written grievance to VCN. Within ten days of receipt, VCN will acknowledge the receipt of the grievance. VCN will promptly notify the participant of the results of its investigation and any corrective action taken. The word "grievance" includes a complaint by a participant regarding the provider-patient relationship. See the section entitled "Summary of Current Examination Results" for further detail.

III. MANAGEMENT AND CONTROL

Board of Directors

The board of directors consists of five members. The bylaws provide that the board shall be elected annually. The board members currently receive no compensation for serving on the board. The board of directors has authorized Dr. Bruce A. Savin to receive a special director's fee, not to exceed \$50,000 annually, without further authorization by the board of directors.

Dr. Savin did not receive this special director's fee in 2004. In 2004, he did receive \$15,000 in dividends. See the section entitled "Summary of Current Examination Results" for further detail.

In addition, board member Adam Savin was paid \$12,300 as a business consultant for services rendered in addition to his work as a board member. See the section entitled "Summary of Current Examination Results" for further detail.

Currently the board of directors consists of the following persons:

Name	Principal Occupation
Dr. Bruce A. Savin	Optometrist
Dr. Robert B. Savin	Retired Optometrist
Dr. Ricki D. Anderson	Optometrist
Adam K. Savin	Business/Computer Consultant / Law Student
Dale P. Rothman-Savin	Artist/Designer

Officers of the LSHO

The officers appointed by the board of directors and serving at the time of this examination are as follows:

Name	Office
Dr. Bruce A. Savin	President / Secretary/ Treasurer

See the section entitled "Summary of Current Examination Results" for further detail.

Committees of the Board

The company's bylaws allow for the formation of certain committees by the board of directors. The only committee at the time of the examination is listed below:

Oversight, Grievance and Quality Committee As of 9/30/2005

Name	Occupation
Bruce A. Savin, O.D. , President	Optometrist
Ricki D. Anderson O.D.	Optometrist
Rona Fatla	Administration / Optician
Michelle Scholes	Administration
Sharon Itzenhauzer	Outside Benefits Manager

VCN has no employees. Necessary staff is provided through a management agreement with Vision Clinic. Under the agreement, effective May 16, 1994, Vision Clinic agrees to perform, but is not limited to, the following services:

1. program planning and development,
2. financial systems and services,
3. provider and subscriber services, including complaint resolution devices,
4. collections and accounts administration, including the recordkeeping required to effectively perform such services.

Per the management agreement, VCN shall pay Vision Clinic "a monthly capitation fee as determined by VCN, to provide both general eye care services, as delineated in the separate Provider Agreement, and general administrative services for VCN. No additional fees shall be paid to Vision Clinic for administrative services rendered to VCN." Ten percent of the monthly capitation fee is allocated to administrative services. See the "Summary of Current Examination Results" for further detail.

The term of the agreement is three years and will automatically renew for an additional three years unless cancelled with no less than 30 days notice prior to the end of the term. Either party may terminate by written notice of intent to terminate mailed at least 90 days prior to the effective date of such termination.

Financial Requirements

The financial requirements for an LSHO under s. Ins 9.04, Wis. Adm. Code, are as follows:

	Amount Required
1. Minimum capital or permanent surplus	Not less than \$75,000
2. Security deposit	Each LSHO is required to maintain a deposit of securities with the state treasurer or an acceptable letter of credit on file with the Commissioner's office. The amount of the deposit or letter of credit shall not be less than \$75,000. The letter of credit must be payable to the Commissioner whenever liquidation or rehabilitation proceedings are initiated against the company.
3. Compulsory surplus	Not less than the greater of: 3% of the premiums earned by the company in the previous 12 months or \$75,000 The Commissioner may accept the deposit or letter of credit under par. 2 to satisfy the compulsory surplus requirement if the company demonstrates to the satisfaction of the Commissioner that all risk for loss has been transferred to the providers.
4. Security surplus	The company should maintain a security surplus to provide an ample margin of safety and clearly assure a sound operation. The security surplus should not be less than 110% of compulsory surplus.
5. Operating funds	Funds sufficient to finance any operating deficits in the business and to prevent impairment of the insurer's initial capital or permanent surplus or its compulsory surplus.

An LSHO which provides hospital services must demonstrate that, in the event of insolvency, enrollees hospitalized on the date of insolvency will be covered until discharge. This does not apply to this LSHO.

The required deposit or letter of credit may satisfy the permanent and compulsory requirement if the LSHO demonstrates that it does not retain any financial loss because all risk has been transferred to the providers. VCN transfers all risk to the providers by reimbursing them on a capitated basis.

VCN has satisfied the financial requirements by the maintenance of a letter of credit, on file with the Office of the Commissioner of Insurance (OCI), in the amount of \$75,000.

VCN is provided with corporate insurance coverage under the contract listed below:

Type of Coverage	Policy Limits
General liability	\$1,000,000 each occurrence 2,000,000 aggregate
Excess liability	3,000,000 each occurrence and aggregate
Auto liability	1,000,000
Worker's compensation Vision Care does not have any employees	0
Personal property Vision Care does not own any personal property	0
Professional liability	1,000,000 each incident 3,000,000 aggregate
Directors' and officers' liability	0

See the section entitled "Summary of Current Examination Results" for further detail.

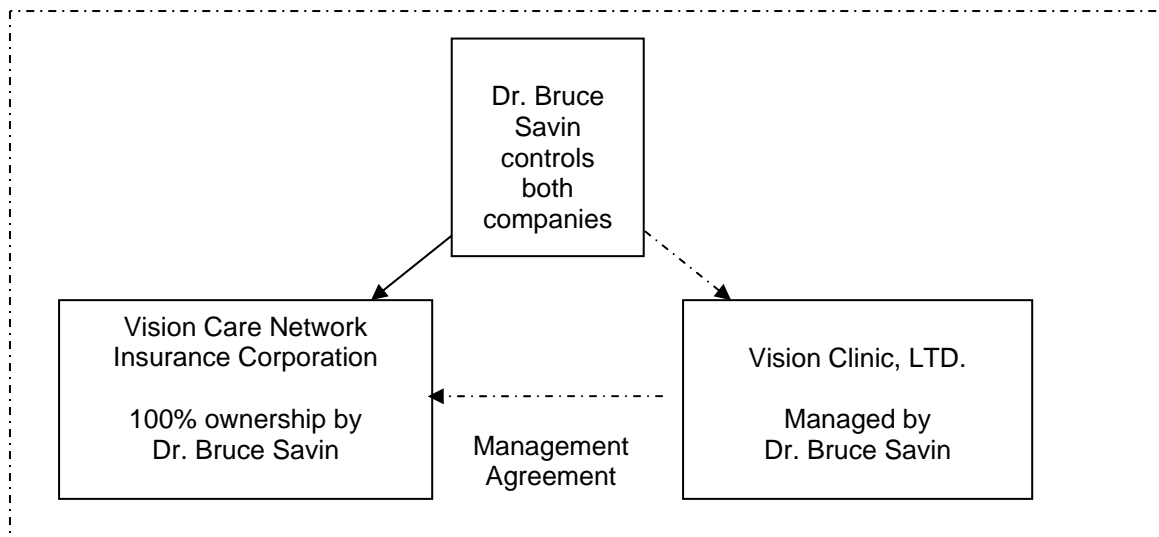
The company is afforded the above coverages through an insurance policy issued in the name of Vision Clinic which specifies that the company is an additional insured certificate holder under the policy in regards to liability coverage only.

IV. AFFILIATED COMPANIES

Vision Care Network Insurance Corporation had not been considered to be a member of a holding company system in the past. However, after further analysis during this examination it was determined that the company does have a holding company relationship with its provider, Vision Clinic, due to the fact that the owner of VCN, Dr. Bruce Savin, is also the manager of Vision Clinic. See the section entitled "Summary of Current Examination Results" for further detail.

The organizational chart below depicts the relationships among the affiliates in the group. A brief description of the significant affiliates of Vision Clinic follows the chart.

**Holding Company Chart
As of December 31, 2004**



Vision Clinic, LTD.

Vision Clinic, LTD., provides vision care services. As of December 31, 2004, the company's unaudited financial statement provided by Dr. Bruce Savin reported assets of \$103,858, liabilities of \$158,569, and Total Stockholder's Equity of (\$54,711). Operations for 2003 produced a loss of (\$44,534) on revenues of \$1,393,725. Operations for 2004 produced a loss of (\$9,553) on revenues of \$1,420,932.

V. FINANCIAL DATA

The following financial statements reflect the financial condition of the company as reported in the December 31, 2004, annual statement to the commissioner of insurance. Also included in this section are schedules which reflect the growth of the company for the period under examination. Adjustments made as a result of the examination are noted at the end of this section in the area captioned "Reconciliation of Net Worth per Examination."

Vision Care Network Insurance Corporation
Assets
As of December 31, 2004

	Assets	Nonadmitted Assets	Net Admitted Assets
Cash, cash equivalents and short-term investments	<u>\$31,541</u>	<u>\$0</u>	<u>\$31,541</u>
Total assets	<u>\$31,541</u>	<u>\$0</u>	<u>\$31,541</u>

Liabilities and Net Worth
As of December 31, 2004

Total liabilities		\$ 0
Common capital stock	\$ 1,000	
Aggregate write-ins for other than special surplus funds	<u>30,541</u>	
Total capital and surplus		<u>31,541</u>
Total liabilities, capital and surplus		<u>\$31,541</u>

Vision Care Network Insurance Corporation
Statement of Revenue and Expenses
For the Year 2004

Net premium income		\$66,076
Medical and hospital:		
Other professional services	\$29,835	
Total medical and hospital	29,835	
General administrative expenses	<u>21,414</u>	
Total underwriting deductions		<u>51,249</u>
Net underwriting gain or (loss)		14,827
Federal and foreign income taxes incurred (refund)		<u>(956)</u>
Net income (loss)		<u>\$15,783</u>

Capital and Surplus Account
As of December 31, 2004

Capital and surplus prior reporting year		\$30,758
Net income or (loss)	\$ 15,783	
Dividends to stockholders	<u>(15,000)</u>	
Net change in capital and surplus		<u>783</u>
Capital and surplus end of reporting year		<u>\$31,541</u>

Statement of Cash Flows
As of December 31, 2004

Premiums collected net of reinsurance		\$ 66,076
Less:		
Benefit- and loss-related payments	\$29,835	
Commissions, expenses paid and aggregate write-ins for deductions	21,414	
Federal and foreign income taxes paid (recovered) \$0 net tax on capital gains (losses)	<u>(956)</u>	
Total		<u>50,293</u>
Net cash from operations		15,783
Dividends to stockholders		<u>(15,000)</u>
Net change in cash and short-term investments		783
Beginning of year (cash and short-term investments)		<u>30,758</u>
End of year (cash and short-term investments)		<u>\$ 31,541</u>

**Vision Care Network Insurance Corporation
Growth of the Company**

The following schedules reflect the growth of the company during the examination

period:

Year	Assets	Liabilities	Capital and Surplus	Premium Earned	Medical Expenses Incurred	Net Income
2004	\$31,541	\$	\$31,541	\$ 66,076	\$29,835	\$15,783
2003	30,758		30,758	98,333	47,316	(9,298)
2002	40,056		40,056	107,952	54,768	18,519
2001	21,537		21,537	107,827	52,748	8,224
2000	13,313		13,313	50,510	24,489	(4,956)
1999	18,269		18,269	58,928	26,361	(966)
1998	20,445	1,210	18,235	80,268	41,166	(1,295)

Year	Profit Margin	Medical Expense Ratio	Administrative Expense Ratio	Enrollment	Change in Enrollment
2004	23.9%	45.2%	32.4%	877 *	-29.7%
2003	-9.5	48.4	58.4	1,248	-3.9
2002	17.2	50.7	31.2	1,298	0.0
2001	7.6	48.9	43.5	1,298	68.6
2000	-9.8	48.5	60.6	770	75.0
1999	-1.6	44.7	56.9	440	-52.4
1998	-1.6	51.3	49.9	925	-80.5

* Extrapolation based on April 22, 2005, correction from the company's accountant – see page 21

Per Member Per Month Information

	2004	2003	Percentage Change
Member months	10,524	14,976	-29.7%
Premium	\$6.28	\$6.57	-4.6
Expenses:			
Hospital/medical benefits	2.83	3.18	-12.3
Total medical and hospital	2.83	3.18	-12.3
General administrative expenses	<u>2.03</u>	<u>3.83</u>	-88.6
Total underwriting deductions	<u>\$4.86</u>	<u>\$7.19</u>	-47.9%

Reconciliation of Net Worth per Examination

The following schedule is a reconciliation of net worth between that reported by the company and as determined by this examination:

Net worth December 31, 2004, per annual statement			\$31,541
	Increase	Decrease	
Current federal and foreign income tax payable and interest thereon	\$	\$(2,290)	
General expenses due or accrued	—	(841)	
Net increase or (decrease)	<u>\$</u>	<u>\$(3,131)</u>	<u>(3,131)</u>
Net worth December 31, 2004, per examination			<u>\$28,410</u>

VI. SUMMARY OF EXAMINATION RESULTS

Compliance with Prior Examination Report Recommendations

Following are the nine specific comments and recommendations contained in the last examination report and subsequent actions taken by the company:

1. Management and Control—It is recommended that the bylaws be amended to indicate the appropriate date of the annual meeting.

Action—Noncompliance

2. Conflict of Interest—It is recommended that the conflict of interest statements reflect the relationship between the board members and VCN's main provider.

Action—Compliance

3. Conflict of Interest—It is recommended that the company obtain original signatures on the conflict of interest statements.

Action—Compliance

4. Contracts—It is recommended that VCN execute a completed contract that indicates the rate to be paid to Vision Clinic.

Action—Noncompliance

5. Contracts—It is recommended that VCN execute a completed contract indicating the percentage of the monthly capitation fee to be applied for administrative services.

Action—Noncompliance

6. Contracts—Pursuant to the NAIC Annual Statement Instructions for Limited Health Service Organization, it is recommended that VCN separate the administrative fee from the provider fee on the annual statement.

Action—Noncompliance

7. Contracts—It is again recommended that the company file with the Commissioner of Insurance all amendments and modifications to its business plan in compliance with s. Ins 3.52 (6), Wis. Adm. Code.

Action—Noncompliance

8. Contracts—It is again recommended that the company submit a revised policy form and certificate of insurance to OCI for approval as required by s. 631.20, Wis. Stat.

Action—Compliance

9. Market Regulation—It is again recommended that, pursuant to s. Ins 3.52 (10), Wis. Adm. Code, the company revise the grievance procedure in the policy to allow for appearance before a grievance panel and provide a procedure for urgent care situations.

Action—Noncompliance

Summary of Current Examination Results

This section contains comments and elaboration on those areas where adverse findings were noted or where unusual situations existed. Comment on the remaining areas of the company's operations is contained in the examination work papers.

Management and Control

Section 617.225, Wis. Stat.; prohibits insurers from paying extraordinary dividends unless the dividend is reported to the commissioner at least 30 days prior to distribution and the commissioner does not disapprove the payment. An extraordinary dividend is defined by s. 601.03 (19), Wis. Stat., as any dividend or distribution of cash or other property, other than a proportional distribution of an insurer's stock, the fair market value of which, together with that of other dividends paid or credited and distributions made within the preceding 12 months, exceeds the lesser of the following:

- (a) Ten percent of the insurer's surplus with regard to policyholders as of the preceding December 31.
- (b) 1. With respect to a life insurer, the total net income of the insurer for the calendar year preceding the date of the dividend or distribution, minus realized capital gains for that calendar year.
2. With respect to an insurer other than a life insurer, the greater of the following:
 - a. The net income of the insurer for the calendar year preceding the date of the dividend or distribution, minus realized capital gains for that calendar year.
 - b. The aggregate of the net income of the insurer for the 3 calendar years preceding the date of the dividend or distribution, minus realized capital gains for those calendar years and minus dividends paid or credited and distributions made within the first 2 of the preceding 3 calendar years.

The examination disclosed that the company paid \$15,000 in 2004, \$13,502 of which are extraordinary dividends as calculated in accordance with s. 600.03 (19), Wis. Stat. The examination also disclosed that the company had no record of reporting the dividend payments as required. It is recommended the company report all dividends at least 30 days in advance as required by ss. 617.22 and 617.225, Wis. Stat.

The examination noted all three company offices (President, Secretary and Treasurer) are being held by one person—Dr. Bruce Savin. Section 611.12 (3), Wis. Stat., states: "Principal Officers - The articles or bylaws shall specifically designate 3 or more offices, the holders of which shall be the principal officers of the corporation. The principal offices shall be

held by at least 3 separate natural persons.” It is recommended the principal offices of the company be held by at least 3 separate natural persons as required by s. 611.12 (3), Wis. Stat.

Insurers are required to report biographical information on directors pursuant to s. 611.54, Wis. Stat., and s. Ins 6.52, Wis. Adm. Code. In April 2004, OCI inquired about deficiencies in the biographical information provided for a new board member (Adam Savin) elected in 2004. Examination noted that these deficiencies still have not been addressed nor has the company responded to the April 2004 inquiry from OCI. This is in violation of s. 601.42, Wis. Stat., which requires the company to promptly respond to the commissioner’s inquiries in writing. In addition, biographical information has not yet been filed for the new (2005) board member, Dale Savin. It is recommended that the biographical data for any new board members be filed in compliance with s. Ins 6.52 (5), Wis. Adm. Code, and, in addition, that the deficient biographical data currently missing be filed within 30 days of adoption of this report.

The prior examination report noted the bylaws indicate that the date of the annual meeting is the first Tuesday in September but that since 1994 the annual meetings have been held in early January. It was recommended that the bylaws be amended to indicate the appropriate date of the annual meeting. During the current examination, it was noted the bylaws have not been updated and the annual meeting has continued to take place in early January. It is again recommended that the bylaws be amended to indicate the appropriate date of the annual meeting.

The examination noted that the company is not in compliance with its own bylaws. The company is paying one of its board members a monthly director’s fee which does not appear to have been approved by the board of directors. The company’s bylaws state "The Board of Directors, by affirmative vote of a majority of the directors then in office, and irrespective of any personal interest of any of its members may establish reasonable compensation of all directors for services to the corporation as directors, officers or otherwise may delegate such authority to an appropriate committee." Based on review of the company’s board of directors and committee minutes review, the compensation paid to this director has not been approved by the board of directors or by a committee. It is recommended that the company comply with its bylaws and seek board approval for compensation paid to any board members.

Contracts

The prior examination report (as of 1998) noted that, upon review of the 1992 examination recommendations, it was reported that the then current management agreement was not filed with OCI. It was also noted that a generic copy of the current master contract, with the updated definition of dependent, was not filed with this office. Pursuant to s. Ins 9.06, Wis. Adm. Code, "all substantial changes, alterations or amendments to the business plan shall be filed with the commissioner at least 30 days prior to their effective date and shall be subject to disapproval by the commissioner." Changes to the business plan includes, but is not limited to, changes to the articles and bylaws, geographical service area, provider agreements, and plan administration. During the prior examination it was again recommended that the company file with the OCI all amendments and modifications to its business plan. The current examination disclosed that the latest provider contract in use at the company is dated 1994 but the latest contract on file with OCI is dated 1989. The company stated that they have not filed with OCI any updates to the provider contract since the last examination as of December 31, 1998. It is again recommended that the company file with the Commissioner of Insurance all amendments and modifications to its business plan in compliance with s. Ins 9.06, Wis. Adm. Code. This is the second repeat of a recommendation from the examination as of December 31, 1992.

The prior examination report noted that VCN pays Vision Clinic a monthly capitation fee and that the provider agreement does not specify the capitation rate. It was recommended that VCN execute a completed contract that indicates the rate to be paid to Vision Clinic. During the current examination, the company confirmed that the contract between VCN and Vision Clinic has not been changed since the last examination as of December 31, 1998. It is again recommended that VCN execute a completed contract that indicates the capitation rate to be paid to Vision Clinic.

The prior examination report noted that, per the management agreement, VCN pays Vision Clinic a monthly capitation fee for eye care services and administrative services. The agreement does not indicate an amount or a percentage of the monthly capitation fee that should be applied to administrative expenses. It was recommended that VCN execute a completed contract indicating the percentage of the monthly capitation fee that should be applied for

administrative services. During the current examination, the company confirmed that the contract between VCN and Vision Clinic has not been changed since the last examination as of December 31, 1998. It is again recommended that VCN execute a completed contract indicating the percentage of the monthly capitation fee that should be applied for administrative services.

The examiners noted that the capitation rate was not consistent from year to year (45%=2004, 48%=2003, 50.7%=2002). When questioned, the company said they review and change the capitation rate every year at the annual board of directors meeting. When the examiner inquired why this rate change was not noted in any of the minutes of the board, the company said it was an oversight. It is recommended that the minutes of the board of directors accurately report capitation rate changes and that rate changes be reported to OCI as amendments to the administration or provider agreements in accordance with s. Ins 9.06, Wis. Adm. Code.

Market Regulation

The prior examination report noted that in the master contract that VCN has with its two primary customers, Twin Disc and Iris; an enrollee is informed of his right to submit a written grievance to VCN and that VCN will acknowledge said grievance within ten days of receipt. The grievance procedure does not indicate the time frame in which VCN will attempt to resolve the matter nor does it indicate the claimant's option to speak to the grievance panel. The grievance procedure also does not provide a procedure for urgent care situations. Although this information is included in the annual grievance report filed with OCI, the information needs to be conveyed in the master contract. The as of 1992 and 1998 examination reports recommended that, pursuant to s. Ins 3.52 (10), Wis. Adm. Code, the company revise the grievance procedure in the policy to allow for an appearance before a grievance panel and to provide a procedure for urgent care situations. During the current examination, it was noted the master contracts with both Twin Disc and Iris have not been revised since 1998 so the recommended grievance procedure changes could not have been made. It is again recommended that, pursuant to s. Ins 3.52 (10), Wis. Adm. Code, the company revise the grievance procedure in the policy to allow for appearance before a grievance panel and to provide a procedure for urgent care situations. This is the second repeat of a recommendation from the examination as of December 31, 1992.

Fidelity Bond

The examination noted that the company does not have the amount of fidelity bond coverage outlined by the NAIC Financial Condition Examiners Handbook. During review of insurance coverage, there was no evidence of officer and directors dishonesty insurance for VCN. When discussed with the company, they could not provide evidence of coverage. It is recommended that the company obtain blanket dishonesty insurance (i.e., fidelity bond) in at least the minimum amounts suggested by the NAIC Financial Condition Examiners Handbook and develop a procedure to ensure the company maintains the minimum level of coverage as suggested by the NAIC.

Cash Disbursements

The examination disclosed that the company pays for 50% of the lease of a car driven by the President. According to s. 611.60, Wis. Stat., material transactions between an insurance corporation and one or more of its directors or officers are voidable unless:

- (a) The transaction at the time it is entered into is reasonable and fair to the interests of the corporation; and
- (b) The transaction has, with full knowledge of its terms and of the interests involved, been approved in advance by the board or by the shareholders; and
- (c) The transaction has been reported to the commissioner immediately after such approval.

The company was unable to provide documentation that the car is used for business and is in the best interest of the corporation. It is recommended that the company no longer pay for a portion of the car lease unless the company can document how the car is used for business, that the lease is reasonable and fair to the interests of the insurer and the company complies with s. 611.60, Wis. Stat.

The examination noted that one of the directors of the board, the President's son, is receiving a monthly "Director's" fee. Examiners inquired with company staff regarding why one director is receiving a "Director's" fee when other directors are not receiving a similar fee. The company responded that this director is providing additional services to the company but could not be specific and could not produce sufficient documentation on what services are being provided and the time spent for these services. This leads to concerns on what, if any, services are being provided to the company and if the "Director's" fee is reasonable and fair to the interests

of the insurer. Section 611.60, Wis. Stat., as described above applies to this transaction as well. It is recommended that the company no longer pay this monthly “Director’s” fee unless the company can document the services provided by the director and document the time spent on these services to show that the fee paid for these services is reasonable and fair to the interests of the insurer and the company complies with s. 611.60, Wis. Stat.

Financial Reporting

The prior examination report noted that, per the management agreement, VCN pays Vision Clinic a monthly capitation fee for eye care services and administrative services. The portion of capitation fees for administrative services is not separated from the provider fees on the annual statement. Pursuant to the NAIC Annual Statement Instructions for Limited Health Service Organization, it was recommended that VCN separate the administrative fee from the provider fee on the annual statement. During the current examination, it was noted the administrative fee and the provider fee have still not been separated on the annual statement. It is again recommended that VCN separate the administrative fee from the provider fee on the annual statement.

In April 2005, OCI inquired whether the number of enrollees (1,248) reported in the annual statement was correct. The company’s accountant replied on April 22, 2005, saying the member months were incorrect—they were reported as 14,827 but should have been 10,524. However, he did not address the number of enrollees and amended schedules affected by this mistake (Five Year Historical Data [page 29], Exhibit 1 [page 17] and Exhibit of Premiums, Enrollment and Utilization [page 30]) were not filed. It is recommended that the company correct any identified errors in its annual statement and promptly file such changes with the commissioner in accordance with the NAIC Annual Statement Instructions – Health.

The examination noted during the review of the company’s federal and state income tax returns that no liability was established in the annual statement for taxes owed on the 2004 income. The company had a payable due to the Internal Revenue Service of \$2,290 and payable due to the Wisconsin Department of Revenue of \$841. This understated liabilities and overstated surplus by \$3,131. The examination adjusted the financial statements for this amount and the adjustment is disclosed in the section of this report captioned “Reconciliation of Net Worth per Examination.” In accordance with NAIC Annual Statement Instructions – Health, a liability should

be established for income taxes due or accrued. Also, Statement of Statutory Accounting Principles (SSAP) No. 10 states a liability should be established for taxes due if it meets the definition of a liability in SSAP No. 5, which defines a liability as “certain or probable future sacrifices of economic benefits arising from present obligations.” It is recommended that the company establish tax liabilities or recoverables in accordance with SSAP No. 10 and in accordance with NAIC Annual Statement Instructions – Health.

Holding Company

Pursuant to ch. Ins 40, Wis. Adm. Code, a holding company system is defined as, “...two or more persons who are affiliates, one or more of which is an insurer.” Pursuant to ch. 600, Wis. Stat., an “affiliate of a person means any other person who controls, is controlled by, or is under common control with, the first person. A corporation is an affiliate of another corporation, regardless of ownership, if substantially the same group of persons manages the two corporations.” The company’s relationship with Vision Clinic, a noninsurer, and the company status as an insurer meet the above definitions of an insurance holding company system. It is recommended that the company or its affiliate annually file an Insurance Holding Company System Annual Registration Statement pursuant to s. Ins 40.03, Wis. Adm. Code.

VII. CONCLUSION

The Vision Care Network Insurance Corporation is a for-profit group model limited service health organization (LSHO) insurer. VCN was incorporated August 8, 1989, and commenced business January 1, 1990. The company currently provides vision care benefits to the employees of two employers. These employers have offered additional vision care options to their employees in recent years resulting in a significant decrease in VCN's enrollment.

The examination made a \$3,131 decrease adjustment to VCN's net worth, reducing it to \$28,410. This adjustment was due to the company's failure to accrue federal and state income tax expense.

There are a total of 17 recommendations, 6 of which are repeat recommendations from the 1998 examination, and 2 of those are repeat recommendations from the 1992 examination.

The company's fortunes are tied to those of the Vision Clinic since the clinic provides all medical and administrative services through agreements with VCN. The clinic has operated at a loss for the past two years reducing its net equity to a negative \$54,711. Management should monitor this situation to ensure that VCN can continue to provide vision care services to its enrollees. The examination recommended that the company file holding company statements. This will allow OCI to monitor the situation as well.

VIII. SUMMARY OF COMMENTS AND RECOMMENDATIONS

1. Page 16 - Management and Control—It is recommended the company report all dividends at least 30 days in advance as required by ss. 617.22 and 617.225, Wis. Stat.
2. Page 17 - Management and Control—It is recommended the principal offices of the company be held by at least 3 separate natural persons as required by s. 611.12 (3), Wis. Stat.
3. Page 17 - Management and Control – It is recommended that the biographical data for any new board members be filed in compliance with s. Ins 6.52 (5), Wis. Adm. Code, and, in addition, that the deficient biographical data currently missing be filed within 30 days of adoption of this report.
4. Page 17 - Management and Control—It is again recommended that the bylaws be amended to indicate the appropriate date of the annual meeting.
5. Page 17 - Management and Control—It is recommended that the company comply with its bylaws and seek board approval for compensation paid to any board members.
6. Page 18 - Contracts—It is again recommended that the company file with the Commissioner of Insurance all amendments and modifications to its business plan in compliance with s. Ins 9.06, Wis. Adm. Code.
7. Page 18 - Contracts—It is again recommended that VCN execute a completed contract that indicates the capitation rate to be paid to Vision Clinic.
8. Page 19 - Contracts—It is again recommended that VCN execute a completed contract indicating the percentage of the monthly capitation fee that should be applied for administrative services.
9. Page 19 - Contracts—It is recommended that the minutes of the board of directors accurately report capitation rate changes and that rate changes be reported to OCI as amendments to the administration or provider agreements in accordance with s. Ins 9.06, Wis. Adm. Code.
10. Page 19 - Market Regulation—It is again recommended that, pursuant to s. Ins 3.52 (10), Wis. Adm. Code, the company revise the grievance procedure in the policy to allow for appearance before a grievance panel and to provide a procedure for urgent care situations.
11. Page 20 - Fidelity Bond—It is recommended that the company obtain blanket dishonesty insurance (i.e., fidelity bond) in at least the minimum amounts suggested by the NAIC Financial Condition Examiners Handbook and develop a procedure to ensure the company maintains the minimum level of coverage as suggested by the NAIC.

12. Page 20 - Cash Disbursements—It is recommended that the company no longer pay for a portion of the car lease unless the company can document how the car is used for business, that the lease is reasonable and fair to the interests of the insurer and the company complies with s. 611.60, Wis. Stat.
13. Page 21 - Cash Disbursements—It is recommended that the company no longer pay this monthly “Director’s” fee unless the company can document the services provided by the director and document the time spent on these services to show that the fee paid for these services is reasonable and fair to the interests of the insurer and the company complies with s. 611.60, Wis. Stat.
14. Page 21 - Financial Reporting—It is again recommended that VCN separate the administrative fee from the provider fee on the annual statement.
15. Page 21 - Annual Statement Reporting Standards—It is recommended that the company correct any identified errors in its annual statement and promptly file such changes with the commissioner in accordance with the NAIC Annual Statement Instructions – Health.
16. Page 22 - Annual Statement Reporting Standards—It is recommended that the company establish tax liabilities or recoverables in accordance with SSAP No. 10 and in accordance with NAIC Annual Statement Instructions – Health.
17. Page 22 - Holding Company—It is recommended that the company or its affiliate annually file an Insurance Holding Company System Annual Registration Statement pursuant to s. Ins 40.03, Wis. Adm. Code.

IX. ACKNOWLEDGMENT

The courtesy and cooperation extended during the course of the examination by the officers and employees of the company are acknowledged.

In addition to the undersigned, the following representatives of the Office of the Commissioner of Insurance, State of Wisconsin, participated in the examination:

Name	Title
Amy Malm	Insurance Examiner

Respectfully submitted,

Glen E. Navis
Examiner-in-Charge